

LOANS AS A MEANS OF FINANCIAL SUPPORT
IN THE VICTORIAN STATE GOVERNMENT'S
CO-OPERATIVE DEVELOPMENT PROGRAM

WORKING PAPER

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This is an initial Working Paper, designed to bring forward for discussion some of the overall structural issues involved in having a system by which loans can be used, as a way of providing financial support to Co-operatives under the Victorian State Government's Co-operative Development Program. It does not attempt to cover the more detailed aspects, such as the desirable level of interest rates, and so on. The Paper was prepared, in particular, for the Victorian State Government's Working Party - which is meeting to consider this topic.

WHY THE NEED FOR LOANS?

At present, all money disbursed by the Co-operative Development Program is by way of a grant. My understanding is that, if a system for making loans was established, then a Co-operative's financial requirements could be satisfied by either a grant, a loan, or by a combination of both. For example, in New South Wales ¹ where loans have been operating for some time, in broad terms, Grant money can be made available for -

- (i) Research and development
- (ii) Initial working capital requirements

and Loan money can be made available for -

- (i) All capital equipment purchases
- (ii) Longer term development and working capital requirements

The following are reasons why it would be desirable to add the Loan Facility to the means of providing financial support to Co-operatives.*

1. By having a loan for part of its financial needs, the Co-operative would be gaining the experience of a normal commercial business in financing its operations.

¹ Appendix III, Paper 1 : New South Wales Beyond June 1982

* Appendix I: Letter outlining necessity of a "Worker Co-operative Bank" in New South Wales.

2. The 'track record' it kept with the lending body could be useful when it came to borrowing from other financial institutions.
3. A loan involves a legal agreement, which gives the lender some claim over the assets of the Co-operative. It must be more attractive - for Government to provide fund money for such things as capital equipment - if it knows that, in the event of a Co-operative's 'winding up', it or its agents can have a chance of recovery.
4. Loans open up the possibility of funds under the Co-operative Development Program being recycled, and used again for the current number of Co-operatives, and/or expansion into helping finance more co-operatives - A Revolving Fund. This would depend, in part, on the way the system of loans was established.
5. It can be noted that the use of loans as a way of financing Co-operatives was part of the original guidelines of the Co-operative Development Program. There have been some difficulties in operating a Loans System within the Ministry of Employment and Training.

THE NEW SOUTH WALES EXPERIENCE

The New South Wales Government has been financing a Co-operative Program since November 1981. As they have also faced the issue of how best to provide financial support for co-operatives - and in particular, have already operated a loans system - what follows is a summary of what I see as being the relevant points for our deliberations. The documents from which the information is drawn are attached, and will be referred to throughout as

Appendix II - The Worker Co-operative Fund, 1981

Appendix III - Beyond June 1982

A. UP UNTIL JUNE 1982

A Submission Review Committee (SRC) ² made the funding recommendations to the Minister, and monitored the co-operatives/groups progress. In the case of

² The Submission Review Committee initially consisted of:

Departmental Advisor, Worker Co-operatives (Chairman)	1 Vote
Administrative Officer, Worker Co-operatives (Secretary)	1 Vote
Financial Consultant, Co-operative Federation of N.S.W.	1 Vote
Management Advisor, WCDC Advisory Unit	Non Voting

Appendix II, Page 3: The Worker Co-operative Fund, 1981

(Continued in Footnotes on Page 3...)

a loan, the SRC gave authority to the Co-operative Federation of N.S.W., to release funds from a 'pool' held by the Federation, on behalf of the Minister. This 'pool' is in the form of a finance company - Common Ownership Finance Company Pty. Ltd.³ These relationships are diagramised in Appendix V.

The SRC worked through the Worker Co-operative Development Committee (WCDC),⁴ which concerned itself with making policy and procedural matters in the Program. Whereas the funding recommendations could not be overturned by the WCDC, those decisions had to be made within the guidelines set down by the WCDC.

Therefore, the Loans System which operated until June 1982, was essentially that the Funding Body (i.e. the SRC), chaired by a Ministry Representative, directed loans to be made from a pool of money which was held in trust on behalf of the Minister, by the Co-operative Federation of New South Wales - (through the Common Ownership Finance Company Pty. Ltd.).

² Submission Review Committee, Continued:

The SRC was later reconstructed, the main change being that the Management Advisor from the Co-operative Advisory Unit represented the Co-operatives at the SRC Meetings, and assisted them in presenting their case for finance (only upon their initiative). It was up to the 'expertise' of the SRC to test any case, and not up to the Business Advisor to 'resource' the Committee. It was felt the old status led to conflict of interest.

The Reconstructed Submission Review Committee:

Departmental Advisor, Worker Co-operatives (Chairman)	1 Vote
Administration Manager, Co-operative Federation of N.S.W.	1 Vote
Outside (Paid) Marketing Consultant	1 Vote

³ One of the reasons for the establishment of the Common Ownership Finance Company Pt. Ltd. - on top of the Co-operative Federation of N.S.W.'s Central Banking System, was to overcome the difficulty that some Worker Co-operatives were Registered as Companies, and the N.S.W. Federation could only operate it's banking facilities for Registered Co-operatives. Apparently, this may not be a problem under the Victorian Legislation. On the other hand, the Co-operative Federation of Victoria does not currently operate Co-operative Banking Facilities.

⁴ Composition of the Worker Co-operative Development Committee:

Departmental Advisor, Worker Co-operatives (Chairman)	1 Vote
Representative Officer, Co-operative Federation of N.S.W.	1 Vote
Three Representatives, Worker Co-operatives in N.S.W.	3 Votes
Business Consultant, Worker Co-operative Development Agency	Non Voting
Education and Training Consultant, WCDA	Non Voting
Administrative Officer, WCDA	Non Voting

Appendix III, Article 1, Page 3: Beyond June 1982

NOTE: The composition and nature of the WCDC has now been altered, as the existing Committee was regarded as having serious flaws. Footnote 6, Page 4.

B. AFTER JUNE 1982

The following are changes to the structure just outlined that were made as from 30th June 1982 -

1. The SRC transferred all of its recommendation powers to the Directors of the Common Ownership Finance Company Pty. Ltd., and then became defunct. The Board of the Company are now empowered to make all decisions on financial assistance - within guidelines, but without individual Ministerial approval. This not only applies to Loan Funds, but also includes Grant Monies.

In March 1982, Grant Funds were placed within the Co-operative Federation of New South Wales, in a Self Help Development Fund, which was operated under instructions from the SRC. This Self Help Fund has now been transferred into the Common Ownership Finance Company Pty. Ltd. and decisions rest with the Board of that Company, the SRC having become defunct.

2. The Minister transferred the Trust Deeds⁵ of the Common Ownership Finance Company Pty. Ltd. to the Co-operative Federation of New South Wales, so that the Federation now owns the funds. The Board of the Company will be appointed by the Federation. The Federation will be directly accountable to the Minister for its operations, funding procedures, and financial arrangements made.

The Worker Co-operative Development Committee (WCDC) still exists, although it has altered in its composition and nature,⁶ to make recommendations to the Ministry on matters of policy and guidelines,

⁵ See Letter of 22nd June 1982: From the New South Wales Minister for Youth and Community Services, to Mr. Freeman, Executive Officer, Co-operative Federation of New South Wales.

Appendix III, Paper 3.

⁶ The new composition of the Worker Co-operative Development Committee:

Departmental Advisor, Worker Co-operatives (Chairman)	1 Vote
Representative Officer, Co-operative Federation of New South Wales	1 Vote
Representative, Worker Co-operatives in New South Wales	1 Vote
Representative, Worker Co-operative Development Agency	1 Vote
Representative, Common Ownership Finance Company Pty. Ltd.	1 Vote

The WCDC's New Charter is in Appendix IV.

and also on the allocation of Funds between -

- (a) The Worker Co-operative Loans System.
- (b) The Self Help Development Fund for research and development of business projects.
- (c) The Worker Co-operative Development Agency, which provides technical and support services.

Therefore, the Co-operative Federation of New South Wales has been made responsible for decisions of financial assistance by way of loans and grants - subject to guidelines developed by the WCDC - and approved by the Minister, and subject to full accountability to the Minister. The Federation has also the responsibility for the monitoring and enforcement conditions attached to those funds disbursed.

It should be noted that the Co-operative Technical Support Services offered through the Worker Co-operative Development Agency, operates quite separately from the Financing System described here. This is in line with the way the now defunct SRC changed its structure so that the Management Advisor of the Business Advisory Service did not have to recommend, or act, as the resource of the Funding Body, due to the conflict of interest. See Footnote 2, Page 3.

Part of the rationale for the change from the situation up until June 1982, and what currently exists, now, appears to be -

1. In the period up until June 30th 1982, the persons entrusted with the Funds (the Co-operative Federation of New South Wales, through the Common Ownership Finance Company Pty. Ltd.) were not also entrusted with the decisions (they acted under the direction of the SRC). Now, the situation exists that the decisions will be made by the Board of the Company, which is entrusted with the Funds, and which will have the necessary expertise of a Financial Institution.

Having made the decisions, and lent Funds, the Financial Institution ought to be in the best position to monitor the financial progress of the Co-operatives to whom it has loaned money - and to enforce its own Contracts in case of default.

Another aspect is that with banking expertise, the Co-operatives could get good advice on the possible risks of their venture - before they get their fingers burnt.

2. Again, in the period up to 30th June 1982, the Funds were in trust to the Co-operative Federation of New South Wales (through the Common Ownership Finance Company Pty. Ltd.), to be held on behalf of the Minister. This meant that the ownership of those Funds rested with the Government - who could conceivably recall them at a later date. By transferring the ownership of the Funds, as was done at 30th June 1982, and therefore eliminating their possible recall, the permanence of the Funds was ensured for the Co-operative purposes outlined by the guidelines. That is, the establishment of a Revolving Fund for Worker Co-operatives in New South Wales.

THE VICTORIAN STATE GOVERNMENT'S CO-OPERATIVE DEVELOPMENT PROGRAM

A. THE CURRENT SITUATION

Although part of the original guidelines for the Co-operative Development Program in Victoria, the use of loans as a means of financing Co-operatives has not yet been used. There have been some technical difficulties in loaning money through the Ministry of Employment and Training.

The current disbursement of Grant money has been facilitated by recommendations of a Funding Committee ⁷ to the Minister. If approved, Funds are then processed through the State Treasury.

The Funding Committee works within guidelines established by the Ministry of Employment and Training's Co-operative Program Unit (CPU).⁸ Apart from policy and procedural matters, the CPU also monitors the progress of the Co-operatives

⁷ Composition of the Funding Committee:

Two Ministry Representatives, Including Chairperson	2 Votes
Managing Director, Small Business Development Corporation	1 Vote
Department of Labour and Industry	1 Vote
Co-operative Federation of Victoria	3 Votes
Registry of Co-operative Societies	1 Vote
Business Advisory Service	Non Voting
Education and Training Unit	Non Voting

⁸ The Co-operative Program Unit (CPU) is comprised of Ministry of Employment and Training Personnel only.

including the financial progress. The Technical and Support Services are provided by the Co-operative Business Advisory Service within the Co-operative Federation of Victoria, and the Co-operative Education and Training Unit, within the Vocational Orientation Centre.

The Co-operative Business Advisory Service - has in the past, and as it currently stands - may make recommendations to the Funding Committee to assist that body make its recommendations on financial and management matters.

The current situation in the Victorian Co-operative Development Program, is in essence, that recommendations for the disbursement of Grant monies are made by a Funding Committee to the Minister, working within guidelines set down by the Minister's Co-operative Program Unit (CPU). The Funds are Budget allocations held by the Treasury, and the monitoring of these funds is done by the Minister's CPU. No loans are currently available.

B. POSSIBLE OPTIONS FOR A LOANS SYSTEM

Assuming the fundamental decision has been made, that loans are a desirable way of providing financial support for Co-operatives under the Co-operative Development Program, the following are some possible options for a Loans System -

- (A) The first set of options are those which most resemble the pre-June 1982 situation in New South Wales, where a Funding 'pool' was established, and operated under the direction of the then existing Funding Recommending Bodies.

OPTION 1.

The Funding Committee makes grant and loan recommendations to the Minister, who then, upon approval, instructs Treasury to establish a Loan Agreement with the Co-operative. In this situation, the Funding 'pool' lies with Treasury. Some of the issues this raises:

- (i) The technical difficulties of the Ministry of Employment and Training making loans, as well as grants, would need to be overcome.
- (ii) There may be practical difficulties involved with the Treasury and loan documentation/timing.

- (iii) Does the Funding Committee have (or can it attract) the necessary ability/expertise to make judgements about loan applications, given that loan decisions tend to increase the accountability of the lender (as well as the borrower). The Funding Committee members are not Bankers, and currently rely, in part, on advice from the Business Advisory Service - which it can be argued strongly - should have its focus on financial and management advice for the Co-operatives; and to also service the Funding Committee, is a conflict of interest. (See Footnote 2, Page 3).
- (iv) Does the Ministry of Employment and Training currently have (or can it attract) the necessary financial expertise to successfully monitor and enforce the loan decisions?

OPTION 2.

The Funding Committee makes grant and loan recommendations to the Minister, who then, upon approval, instructs the State Bank (please take 'State Bank' to read: An existing, or potential, Financial Institution - other than the Federation of Victoria - such as the Victorian Economic Development Committee, or the Small Business Development Corporation) to establish a Loan Agreement with the Co-operative. The Funding 'pool' in this situation lies with the State Bank. Some of the issues this raises:

- (i) This could be a way of getting around the technical difficulties that the Ministry of Employment and Training may have, with making loans.
- (ii) Being Bankers, the State Bank Option may also ease the burden with Treasury in the practical aspects of lending - documentation/time.
- (iii) The issue of financial expertise (or its ability to attract it) of the Ministry and the Funding Committee still exists under this Option, as the State Bank is merely operating a Fund 'pool' under instructions from the Ministry.
- (iv) In this situation, the financial support for the Co-operatives could come by way of grant from Treasury, and by way of loan from the Funding 'pool'.

OPTION 3.

The Funding Committee makes grants and loan recommendations to the Minister, who then, upon approval, instructs the Co-operative Federation of Victoria to establish a Loan Agreement with the Co-operative. The Funding 'pool' in this situation, lies with the Co-operative Federation of Victoria - the Funds being held in Trust on behalf of the Minister. (This Option most closely resembles the pre-June 30th 1982 New South Wales situation.) Some of the issues this raises:

- (i) This, again, could be a way of getting around the technical difficulties that the Minister of Employment and Training may have with making loans.
 - (ii) The Victorian Federation,⁹ unlike it's New South Wales counterpart, does not currently have operating a Co-operative Banking System, and therefore would need to overcome the practical aspects of lending. Being non-governmental, this may be easier to do than, say, for Treasury.
 - (iii) The issue of financial expertise (or it's ability to attract it) of the Ministry and the Funding Committee still exist under this Option, as the Co-operative Federation of Victoria is merely operating a Fund 'pool' under instructions from the Ministry.
 - (iv) Again, in this situation the financial support for the Co-operative could come by way of grant from Treasury, and by way of loan from the Funding 'pool'.
- (B) It is important to stress that the three Options in the first set of Options do not adequately tackle the following two issues -
- 1. Because the Fund 'pool' is operated under instruction, it means that the persons entrusted with the Funds are not also entrusted with the decisions to lend. If the monitoring and enforcement of Loan Funds is to be done effectively, it would seem highly desirable that the decision makers - those entrusted with the Funds and those who need to monitor and enforce - be one and the same Organisation.

⁹ The Legislation allows the Federation of Victoria to offer its facilities to co-operatively constituted companies, and therefore the need to establish a separate company like the Common Ownership Finance Company would not be necessary.

2. In the three Options outlined so far, the Ownership of the Funds remained with the Government - either through the Treasury, or to be held in Trust on behalf of the Minister by the State Bank, or the Co-operative Federation of Victoria. This, therefore, leaves open the possibility of recall of these Funds at a later date - or instructions to disburse with the Funds at a greater rate than is appropriate for a Lending Institution. In order to ensure the continual availability of those Funds for the purpose set out by the guidelines - A Revolving Fund for Co-operatives - it would appear that the Ownership of the Funds would need to be transferred outside the Government - with full accountability to the Minister for operations, funding procedures, and financial arrangements made.

The second set of Options that follow do tackle the two issues just outlined, and these Options most resemble the New South Wales Loans System, operating after the 30th of June 1981.

OPTION 4.

The Co-operative Federation of Victoria establishes a 'Banking' Facility to which the Minister grants Funds. The Federation be empowered to make Funding decisions with those Funds, within the guidelines approved by the Ministry. The Federation would be directly accountable to the Minister for its operations, funding procedures, and financial arrangements made. Some of the issues this raises:

- (i) This, again, would be a way of overcoming the technical difficulties that the Ministry of Employment and Training may have with making loans.
- (ii) As indicated above, the Co-operative Federation of Victoria does not have, and would therefore have to establish, a 'Banking' Facility to cope with the practicalities of lending. Being non-governmental, this may be easier to do than, say, for Treasury. This raises the issue of what other 'Banking' Facilities are available to Co-operatives as a whole - both currently, and planned for the future - and the relationship of the Co-operatives in the Program to these Facilities.

- (iii) Because this Option actually puts the decision-making power with the Federation as Owners of the Funds, it potentially means that 'banking' expertise can be attracted to make Funding decisions, assess progress, and enforce their own Contracts. The exact constitution of this decision-making body - and in particular, it's relationship to Co-operatives in the Program - would need examination.
- (iv) With this Option, it seems necessary that the Funding decisions imply grants, as well as loans, as it would be cumbersome to have two decision-making bodies. Therefore, the grant to the Federation from the Minister could consist of an allocation for grants, and another for loans.
- (v) As the Ownership of the Funds would now be granted outside of Government, the Loan Funds would be in perpetuity for Co-operatives, under established guidelines - A Revolving Fund.
- (vi) With the guidelines and policy for the operation of the Federation's 'Banking' Facility being determined by the Minister, it may be necessary to consider the expansion of the Ministry of Employment and Training's Co-operative Development Program Unit, or the development of a new body along the lines of the Worker Co-operative Development Committee (WCDC) in New South Wales (Footnote 6, Page 4), by which to increase representation by more of the parties involved in the Program, than with the current Co-operative Program Unit.
- (vii) As the Co-operative Federation of Victoria currently hosts the Business Advisory Service as one of the technical arms of the Program, I submit that this would not be incompatible with operating a 'Banking' Facility, if kept completely separate. (See Footnote 1, Page 1).

By way of Note: The Interest earned on the Fund Pool can contribute towards the financing of a Loans Officer, and procuring additional advice for the Board of Directors, where necessary.

OPTION 5.

As in Option 4, but for the fact that the Minister grants funds to a Body other than the Co-operative Federation of Victoria, such as the State Bank. Some of the issues this raises:

- (i) This Option would fulfill all of the Points under Option 4, and it may be possible to locate an existing Banking Facility, such as the State Bank, which would overcome the current inexperience of the Federation at this time. However - the Co-operative Federation of Victoria is in the business of Co-operatives, and is in touch with the needs of developing Co-operatives. This could be extremely important in following the guidelines, and in making Funding decisions. The Co-operative Federation of Victoria is Incorporating itself directly under the new 1982 Co-operation Act.